84207-8

COA NO. 39517-7

No. 82127-5

SUPREME COURT
OF THE STATE OF WASHINGTON

FLIGHT OPTIONS LLC,

Petitioner,

v.

WASHINGTON DEPARTMENT OF REVENUE,

Respondent.

APPELLANT ~~PETITIONER~~ FLIGHT OPTIONS' OPENING BRIEF

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INTRODUCTION

The Department of Revenue's unprecedented assessment of property taxes against Flight Options LLC for jets that it does not own but has sold in undivided ownership interests to third parties violates elemental aspects of Washington tax law. This Court has long held that property tax liability attaches only to the owner of the assessed property. Moreover, the statute under which the Department purports to act limits property tax assessments to the taxable property's owner.

The assessment also violates the requirement that property must possess a taxable situs in the taxing district. The privately-owned jets at issue in this case are domiciled outside of the state and enter Washington, if at all, only temporarily on an irregular and unscheduled basis at the whim of the fractional owner; consequently, they do not have a permanent presence within the state that would establish a taxable situs.

Finally, the Department seeks to re-write Flight Options' sales and management agreements with the planes' fractional owners in an attempt to characterize Flight Options as a "common carrier by air" subject to Department's statutory central assessment power. However, Washington law prohibits the Department from imputing activities to Flight Options in order to improperly expand its jurisdiction.

Unfortunately, the Superior Court fundamentally mischaracterized and failed to address these critical issues. Therefore, Flight Options seeks relief from this Court.

ASSIGNMENTS OF ERROR

A. Assignments of Error

1. The trial court erred in opining that Flight Options could be subject to a commercial utilities excise tax rather than addressing Flight Options' objections to the Department's assessment of property tax.

2. The trial court erred in basing its ruling on a United States constitutional provision – the Commerce Clause – that is not at issue in this case.

3. The trial court erred in failing to decide, or even address, the Washington law and due process issues that are central to this lawsuit.

B. Issues Pertaining to Assignments of Error

1. Does Washington State law require that the Department of Revenue assess property taxes against the owner of the taxed property? (Assignments of Error 1 and 3.)

2. Does movable property domiciled outside Washington obtain a tax situs in Washington if it temporarily enters the state on an irregular and unscheduled basis? (Assignments of Error 1, 2, and 3.)

3. Is a company that sells private jets to fractional owners an inter-county public utility, and therefore, subject to the Department's authority to centrally assess and allocate the value of its multi-county operating property among the various Washington counties in which the property is situated? (Assignments of Error 1 and 3.)

STATEMENT OF THE CASE

A. Factual Background

Flight Options is a leading seller of fractional ownership interests in private corporate jets. CP 33. Flight Options is a Delaware limited liability company with its headquarters and principal place of business in Richmond Heights, Ohio. *Id.* It does not maintain an office, place of business, or operations in Washington. CP 35.

Flight Options purchases corporate jets that it re-sells to private owners in fractional shares. CP 34; *see also* CP 129-44 (Flight Options Purchase Agreement). These purchasers acquire title and an undivided ownership interest in a specific aircraft and the Federal Aviation Administration recognizes the purchasers as legal owners of a partial interest in the particular aircraft. CP 34. Each fractionally-owned jet has between two and sixteen owners. *Id.* Flight Options also provides management services to the owners of the airplanes under a separate agreement and monthly fee. CP 34-5; *see also* CP 146-65, 167-87 (2004 and 2005 Flight Options Management Agreements).

The privately-owned jets managed by Flight Options do not operate on fixed routes or regular schedules. CP 35. Rather, the owners use their aircraft to fly at-will between airfields throughout the United States and internationally. *Id.* None of the jets are hangared in Washington. *Id.* If a jet managed by Flight Options enters Washington, it

does so only temporarily on an irregular and unscheduled basis at the direction of a fractional owner.[1]

B. Procedural History

On June 8, 2005, the Department emailed Flight Options an "Airplane Company Annual Report" and instructed Flight Options to file it before June 30, 2005, "to avoid a default assessment and 25% penalty." CP 715. When demanding that Flight Options submit the report, the Department instructed Flight Options to list "all aircraft in the fractional program . . . under the 'owned' category." *Id.* To avoid the threatened penalty, Flight Options provided the information demanded by the Department. CP 36.

Flight Options thereafter challenged the Department's authority to issue the assessment by filing this suit for declaratory and injunctive relief on January 6, 2006, in Thurston County Superior Court. After the Department issued a second assessment later that year, Flight Options amended the complaint to include that assessment as well. CP 4. Both assessments allocated tax exclusively to King County. CP 37. Following completion of discovery, the parties filed cross motions for summary judgment. CP 94, 206.

On July 10, 2008, the Superior Court issued a letter opinion dismissing Flight Options' challenge to the validity of the Department's property tax assessment on the basis that a "commercial utilities tax" on

[1] A small percentage of flights are made by members of Jet Pass, a private membership program that provides access to private jets without ownership.

Flight Options' activities is not barred by the Commerce Clause. CP 740. In its decision, the Superior Court: (a) stated that it was adjudicating "public utility taxation" with no mention of property taxes, (b) based its ruling on the Commerce Clause, and (c) did not address the Washington property tax law and due process issues raised in this lawsuit. CP 740-42. On August 19, 2008, the Superior Court formally issued its Order on Cross-Motions for Summary Judgment. CP 743. Flight Options timely filed a notice of appeal. CP 749.

ARGUMENT

The Department's assessment of property taxes against Flight Options for privately-owned jets was erroneous and should be invalidated because: (1) personal property taxes are imposed only against the owner of the taxed property; (2) personal property is taxable only at its situs, normally the owner's domicile, and irregular and unscheduled flights at the whim of fractional owners do not establish a permanent presence that would alter the situs; and (3) the Department may not re-characterize a taxpayer as an "inter-county public utility" engaged in a public service business in contravention of controlling contractual language.

A. Property Taxes May Only Be Assessed Against the Owner of the Taxed Property.

In distinguishing between property and excise taxes, this Court has explained that property taxes are imposed on "the ownership of property," such that liability arises from the taxpayers' "status as property owners." *Covell v. City of Seattle*, 127 Wn.2d 874, 890, 905 P.2d 324 (1995). To that end, Washington statutes imposing personal property tax liability specifically require that the property be "assessed . . . with reference to its value and ***ownership*** on the first day of January of the year in which it is assessed." RCW 84.40.020 (emphasis added). In construing RCW 84.40.020, the Court of Appeals has held that "[o]wnership and not possession is taxable." *Star Iron & Steel Co. v. Pierce County,* 5 Wn. App. 515, 525, 488 P.2d 782 (1971) (in enjoining an assessment of

property taxes against a person who was not the owner of the property subject to tax).[2]

The Department's assessment of property taxes against Flight Options in this case violated this basic tenant of Washington tax law. As the Department has conceded, Flight Options did not own over 80 percent of the property for which the Department assessed property taxes against it. *See, e.g.,* RP (5/16/08) at 54:14-15. Indeed, the Purchase Agreement executed between Flight Options and a private jet owner is unambiguous: "Buyer desires to purchase from Seller, and Seller desires to sell to Buyer an undivided interest in the Aircraft." CP 129. The agreement expressly recognizes that after selling each of the jet's fractional shares, the various interest owners "shall own in the aggregate exactly 100% of the Aircraft." CP 136. Moreover, the separate Master Interchange Agreement specifically states that it is "an arrangement whereby a Participant ***leases his airplane*** to another Participant in exchange for equal time, when needed, on the ***other Participant's airplane***." CP 191 (emphasis added). Once a sale occurs, the Federal Aviation Administration recognizes that the purchasers have acquired title as the legal owner of an undivided ownership interest in a specific aircraft. CP 34

Moreover, even if Flight Options were an inter-county public utility (which, as discussed in Section C below, it is not), the Department

[2] The nature of property taxes and the method to enforce their collection also compels this result. To enforce the payment of property taxes, the Department places a lien on the relevant property. As this Court has held, however, it is unconstitutional to foreclose a tax lien against property owned by someone other than the taxpayer. *State v. Lawton*, 25 Wn.2d 750, 764-65, 172 P.2d 465 (1946).

would still be required to assess property taxes based on ownership. Washington law provides the Department with authority to centrally assess property taxes of inter-county public utility companies. *See generally* Ch 84.12 RCW. The statute confirms, however, that "property used but not owned by an operating company . . . shall be deemed the sole operating property of the owning company." RCW 84.12.120. Thus, in *Canadian Pacific Railway Company v. King County*, 90 Wn. 38, 144 P. 416 (1916), this Court held that any property tax due on railroad cars *operated by* the Northern Pacific Railroad in Washington State was required to be assessed against the ***owner*** of the cars, Canadian Pacific, ***not the operator***. *Id.* at 45-46.

In its brief letter opinion, the Superior Court erred in opining that Flight Options could be subjected to a commercial utilities excise tax. CP 740. This case involves a property tax assessment, not an excise tax. This Court has previously highlighted the critical distinction between ***property taxes*** imposed upon a taxpayer's ***ownership*** of property and ***excise tax***es based on a taxpayer's ***activities***. *Covell*, 127 Wn.2d at 889-90 (citing *High Tide Seafoods v. State,* 106 Wn.2d 695, 699, 725 P.2d 411 (1986)). Unfortunately, the Superior Court failed to analyze or even address this issue in its opinion. CP 740-42. Instead, the court inexplicably upheld the Department's assessment even though it determined that Flight Options did not own 80 percent of the jets that were assessed. CP 741. That ruling is inconsistent with established Washington tax law and, therefore, Flight Options requests that this Court reverse the Superior Court's order.

B. The Department's Property Tax Assessment Against Flight Options Was Improper Because the Jets Lacked the Requisite Tax Situs in Washington.

The Superior Court's order granting summary judgment to the Department should be reversed because the court failed to address another fundamental and controlling aspect of Washington law, namely, that tangible property may be taxed only in the jurisdiction of its situs. The court also did not discuss similar requirements arising under the Due Process Clause of the U.S. Constitution, instead determining that the "tax imposed passes constitutional muster" under the "commerce clause." CP 741. However, Flight Options has not challenged the Department's assessment under the Commerce Clause. As discussed below, the Department's position that the temporary presence of some private jets on an irregular and unscheduled basis creates a tax situs in Washington for all private jets managed by Flight Options is contrary to established Washington law and due process principles, each of which provides a separate basis for reversal.

1. Under Washington law, the temporary presence of property on an unscheduled and irregular basis does not create a tax situs

In Washington, "[t]he law is well settled that tangible personal property is subject to taxation in the jurisdiction in which it has its actual situs." *U.S. Whaling Co. v. King County*, 96 Wn. 434, 436, 165 P. 70 (1917); Wash. AGO 1929-30, pg. 179 ("Tangible personalty is taxable in this state at its situs.") This principle has been codified by statute. RCW 84.44.010 (personal property shall be assessed "in the county where it is

situated").[3] "Personal property has its situs at the domicile of the owner." *In re Grady's Estate*, 79 Wn.2d 41, 43, 483 P.2d 114 (1971). When property is permanently present somewhere other than the owner's domicile, its situs may shift to that place. Wash. AGO 1923-24, pg. 239-40 (citing *Town of Uniontown v. Klemgard*, 129 Wn. 144, 224 P. 610 (1924)); *Guinness v. King County*, 32 Wn.2d 503, 507, 202 P.2d 737 (1949) (a nonresident's property is subject to another state's property tax if it is "used or employed permanently there"); *Cent. R.R. Co. of Pa. v. Pa.*, 370 U.S. 607, 611-12, 82 S. Ct. 1297, 8 L. Ed. 2d 720 (1962) ("[T]he State of domicile retains jurisdiction to tax tangible personal property which has 'not acquired an actual situs elsewhere.'") (quoting *Johnson Oil Refining Co. v. Okla.*, 290 U.S. 158, 161, 54 S. Ct. 152, 78 L. Ed. 238 (1933)).

This Court has examined the distinction between permanent and temporary presence within Washington State sufficient to create a tax situs different from the owner's domicile. *Guinness*, 32 Wn.2d at 506-07. In *Guinness*, the putative taxpayer, whose domicile was in London, sailed his yacht along the United States' and Canadian coastline before mooring it in Seattle and returning home. *Id.* at 505. When Great Britain declared war

3 "There is nearly universal agreement that personal property is 'situated' for tax purposes at its tax situs, which requires a sufficient nexus between the property and the taxing jurisdiction." *Mesa Leasing Ltd. v. City of Burlington*, 169 Vt. 93, 96, 730 A.2d 1102 (1999) (citations omitted); *see also Zantop Air Transp. v. San Bernadino County*, 246 Cal.App.2d 433, 437, 54 Cal.Rptr. 813 (1966) ("The word 'situated' . . . is synonymous with 'situs.'"); *J.H. Berra Constr. v. Jefferson County Assessor*, 2003 WL 1964029 (Mo. St. Tax Comm'n 2003) ("'Situated' is synonymous with 'situs' and denotes a more or less permanent location.") (citing *Buchanan County v. State Tax Comm'n*, 407 S.W.2d 910 (Mo. 1966)).

against Germany shortly thereafter, emergency British legislation "froze" the yacht in Seattle until the end of the war. *Id.* at 505, 508. In determining that the yacht's presence during the five-year war was temporary, this Court held, as a matter of Washington law, that tax situs over a nonresident's moveable tangible personal property requires "permanent presence" within the State. *Id.* at 507. By contrast to such "permanent presence," this Court further explained that:

> '[C]hattels merely temporarily or transiently within the limits of a state are not subject to its property taxes. ***Tangible personal property passing through or in the state for temporary purposes only***, if it belongs to a nonresident, ***is not subject to taxation*** under a statute providing that all real and personal property in the state shall be assessed and taxed. ***The state of origin remains the permanent situs*** of property for the purpose of taxation, notwithstanding the occasional excursion of the property to foreign parts.'

Id. (quoting 51 Am. Jur. 468, Taxation § 453) (emphasis added).

This distinction between permanent and temporary presence sufficient to establish a tax situs is consistent with this Court's decision in *Canadian Pacific*. In that case, King County assessed property taxes against a Canadian company for its railroad cars that a Washington company, Northern Pacific, was using to provide daily scheduled service between British Columbia and Seattle. *Canadian Pac.*, 90 Wn. at 39-40. The agreement between the two companies stated that Canadian Pacific would provide three passenger cars for daily use by Northern Pacific on a fixed route and schedule within Washington State. *Id.* at 40-41. While

Canadian Pacific's domicile was in Canada, this Court held that three railway cars could be assessed by King County. *Id.* at 45. In reaching this determination, the court relied on the fact that it was "conclusively established" that (1) appellant owned cars that followed "certain routes of travel," (2) the cars were "regularly used and employed in railroad business within this State," and (3) "the same number of cars [we]re used daily." *Id.* at 44. In other words, in Washington, mobile personal property that temporarily enters the state obtains sufficient "permanent presence" to establish a tax situs through regular use on fixed travel routes and schedules.

Under Washington law, as discussed in *Guinness* and *Canadian Pacific*, the private jets managed by Flight Options did not acquire a tax situs through the sporadic, transitory presence of some of those jets within the state at the whim of individual fractional owners. Unlike the railroad cars in *Canadian Pacific*, it is undisputed that this case does not involve any planes flying into Washington on fixed routes or schedules. CP 35. Moreover, in *Canadian Pacific* a fixed number of railroad cars were permanently present in the State (since cars traveling to Seattle remained there overnight to return on the next day's Vancouver route). *Canadian Pac.*, 90 Wn. at 40. By contrast, the privately-owned jets here enter Washington at the direction of owners (who select the unscheduled destinations) and are on the ground long enough to only load or unload the plane. CP 35. Since the jets do not have a "permanent presence" in Washington sufficient to establish a tax situs, the situs of each fractional

ownership interest remains at the individual owner's domicile. As a result, any Washington resident with a fractional interest in a jet managed by Flight Options would be subject to property tax by the County Assessor in the county where that owner resides.

2. Other states have agreed with Washington that a non-resident's personal property requires a permanent presence to establish a tax situs other than the owner's domicile.

Other state supreme courts have considered the specific issue of the property tax situs of aircraft and have applied the same analysis as this Court. *Flying Tiger Line, Inc. v. Bd. of Assessors of Boston*, 404 Mass. 359, 535 N.E.2d 231 (1989); *Peabody Coal v. State Tax Comm'n*, 731 S.W.2d 837 (Mo. 1987).

In the most analogous case decided under state law, a Missouri business that owned two private jets and used them to fly between "its several installations" argued that the aircraft had "acquired a taxable situs in Indiana[] by reason of their frequent landings there." *Peabody*, 731 S.W.2d at 838. Respectively, the two aircraft made 32 percent and 20 percent of their landings in Indiana. *Id.* The court held that the jets had not acquired a taxable situs in Indiana because the unscheduled and irregular landings there, while frequent, did not exhibit the "continuous presence" necessary to establish taxable situs. *Id.* at 839. In arriving at its decision, the court contrasted the case with a situation involving "fixed routes and regular schedules." *Id.* at 838. Similar to the rule expressed by this Court in *Guinness* and *Canadian Pacific*, the Missouri Supreme Court

expressed the need for continual presence amounting to permanence to establish a taxable situs:

> To acquire an 'actual situs' in another state so as to limit the exclusive taxing authority of the home state, ***there must be 'continuous presence*** in another state which thereby supplants the home state and acquires the taxing power over personalty ***that has become a permanent part of the foreign state.***'

Id. at 839 (quoting *Northwest Airlines, Inc. v. Minn.*, 322 U.S. 292, 296, 64 S. Ct. 950, 952, 88 L. Ed. 1283 (1944)) (emphasis added).

In *Flying Tiger*, the Massachusetts Supreme Court addressed whether aircraft owned by two Delaware corporations that used Logan International Airport had acquired a taxable situs in Boston. *Flying Tiger*, 404 Mass. at 360. The aircraft were "regularly" present in Boston, albeit for only "brief" periods of time. *Id.* at 364. In construing a statute imposing tax on property "situated" in Boston, the court stated that "[t]o be situated in a municipality[,] the property must have 'some degree of permanence of location' and 'temporary lodgment or migratory presence' is not enough." *Id.* (quoting *Carlos Ruggles Lumber Co. v. Commonwealth*, 261 Mass. 445, 448, 158 N.E. 897 (1927)). Applying this test, the court held that the "brief but regular presence" of the aircraft in Boston "lack[ed] sufficient permanence" to establish a taxable situs. *Id.*

The state supreme courts in both *Peabody* and *Flying Tiger* employed the permanent presence test applied by this Court in *Guinness* and *Canadian Pacific*. Under this principle, which the Superior Court failed to even acknowledge let alone address, the privately-owned jets

managed by Flight Options did establish a tax situs in Washington State. It is undisputed that the privately-owned jets managed by Flight Options do not operate on "fixed routes and regular schedules." CP 35. Their sporadic and unscheduled presence in any Washington county in which they happen to have been directed by fractional owners can be described only as "brief."

3. Under the Due Process Clause, movable property does not acquire a taxable situs elsewhere unless it operates on fixed routes and regular schedules.

In arriving at its decision, the Superior Court failed to recognize that the Due Process Clause of the United States Constitution and state law provide ***separate*** restrictions on the assessment of property taxes. CP 740-42. The court did not even address Washington property tax law or the Due Process Clause, instead determining that a "commercial utilities tax" on Flight Options "passes constitutional muster" under the "commerce clause." *Id.* However, the U.S. Supreme Court has affirmed injunctions against property tax assessments that are not authorized by state law, without regard to whether the assessment might be within the limitations imposed by the Due Process Clause. *Marye v. Balt. & Ohio R.R. Co.*, 127 U.S. 117, 124, 8 S. Ct. 1037, 32 L. Ed. 94 (1888). The U.S. Supreme Court has also clarified that the federal constitutional issue as to whether movable property "has tax situs in a state for the purpose of subjection to a property tax is one of due process." *Braniff Airways, Inc. v. Neb. State Bd. of Equalization*, 347 U.S. 590, 599, 74 S. Ct. 757, 98 L. Ed. 2d 967 (1954). Properly applied, the separate requirements of the Due Process

Clause further support the determination under Washington law that the Department lacked authority to assess property taxes against Flight Options for the private jets owned by others that only entered Washington, if at all, sporadically on an unscheduled basis as directed by the owners.

In three critical decisions, the U.S. Supreme Court has outlined the scope of the restrictions imposed by the Due Process Clause on the assessment of property taxes on personal property in a state other than the owner's domicile. *Cent. R.R.*, 370 U.S. 607; *Braniff Airways*, 347 U.S. 590; *Northwest Airlines*, 322 U.S. 292. First, in *Northwest Airlines*, the Court affirmed that the Due Process Clause does not bar a domicile state from fully taxing an owner's interest in personal property unless the property has become "permanently situated" in another state. *Northwest Airlines*, 322 U.S. at 297-98. Northwest Airlines had challenged Minnesota's property tax assessment of its entire fleet, which regularly flew between eight different states. *Id.* at 293. Notwithstanding evidence that every plane in the fleet routinely left Minnesota – Northwest's domicile state – on routes to other destinations, the Court found that "it is not shown here that a defined part of the domiciliary corpus has acquired a permanent location, i.e., a taxing situs, elsewhere." *Id.* at 295. Due to this lack of "permanence" in another state, the court held that Minnesota retained exclusive authority to impose property taxes on the aircraft. *Id.*

In *Braniff Airways*, the Court did permit a non-domicile state (Nebraska) to tax a portion of an airline's fleet where the company permanently employed a portion of the fleet and operations there, creating

a taxable situs. The Court clearly stated that this determination flowed from the Due Process Clause, not the Commerce Clause. *Id.* at 598-99. Braniff Airways established such a permanent presence by "operating over fixed routes and landing on and departing from airports within Nebraska on fixed schedules" and maintaining ground operations at the two Nebraska airports served by these regularly scheduled flights. *Braniff Airways*, 347 U.S. at 591. While the Court permitted non-domiciliary property taxation in *Braniff Airways* and not *Northwest Airlines*, the Court stressed that *Northwest Airlines* remained valid and distinguished the two cases, emphasizing that the evidence in the latter (as in this case) had not shown a permanent presence in a non-domicile state. *Id.* at 601-02.

In *Central Railroad*, the Court affirmed the distinction established by these earlier cases, noting that "[i]n *Braniff*, the airplanes held subject to non-domiciliary taxation were shown by the record to have flown on ***fixed and regular routes***." *Cent. R.R.*, 370 U.S. at 617 (emphasis added). Applying this principle of due process, the Court held that 158 railroad cars owned by a Pennsylvania company but operated on "fixed routes and regular schedules" in New Jersey had acquired a tax situs in New Jersey. *Id.* at 613. As a result, Pennsylvania could not, as a constitutional matter, continue to include them in its property tax assessments. *Id.* at 614. However, the Court also determined that the company's other 1,507 railroad cars that were "regularly, habitually and/or continuously employed" outside Pennsylvania nevertheless retained their tax situs in

that state because "they did not run 'on fixed routes and regular schedules.'" *Id.*

The due process tax situs principles addressed in these three U.S. Supreme Court decisions are consistent with the permanent presence requirement applied in this Court's decision in both *Guinness* and *Canadian Pacific* (and *Peabody* and *Flying Tiger*). *Central Railroad* and *Braniff Airways* establish that movable personal property can acquire a non-domiciliary tax situs only where the property moves on "fixed routes and regular schedules" in the taxing district. All three cases demonstrate that movable property that makes temporary stops on a recurring basis in the district does not establish the permanent presence necessary to acquire a taxable situs in the absence of fixed routes and regular schedules.

Here, the sporadic and irregular presence of private jets in Washington at the direction of various fractional owners falls well short of the permanent presence bar set in *Northwest Airlines*, *Braniff Airways*, and *Central Railroad*. By contrast to *Braniff Airways* and *Central Railroad*, there are no fixed schedules for flights into Washington and Flight Options neither owns nor leases ground facilities at any Washington airfield. CP 35. Any fractionally-owned jet that enters Washington does so only on an intermittent basis,[4] and thus, the Superior Court erred in determining that the Department's assessment was valid.

[4] In *Braniff Airways*, the U.S. Supreme Court noted that Nebraska attempted to assess property taxes "only against regularly scheduled air carriers and . . . not . . . carriers who operate only intermittently." *Brainiff Airways*, 347 U.S. at 592-93.

Additionally, even if the Department's assessment of property taxes against Flight Options "passed constitutional muster," which it does not, such constitutional permissibility does not control the question as to whether it is authorized under Washington law. Washington's situs requirement does not rely on federal due process principles and is a separate bar that the Department has failed to meet.

C. The Department lacked Authority to Assess Property Taxes Against Flight Options Under Ch. 84.12 RCW Because Flight Options Is not an Inter-County Public Utility Company Subject to Central Assessment Under that Chapter.

Not only did the Department's assessment violate Washington State property tax law and federal due process principles, but it also disregarded the actual contracts between Flight Options and the fractional owners. The Department has attempted to re-characterize Flight Options as a "common carrier" airline company subject to taxation as an "inter-county public utility company." CP 105-08. As discussed below, Washington law does not permit the Department to impute activities to Flight Options in contravention of its contracts with the fractional owners.

The Department's proffered substance over form theory for assessing property taxes in this case is that, despite the clear language of Flights Options' contracts, "the fractional ownership program is really a method of selling air transportation." CP 104. However, this Court has held that the Department has "no authority" under Washington law to "impute" activity to a taxpayer contrary to the actual terms of the taxpayer's contracts. *Weyerhaeuser Co. v. State Dep't of Revenue*, 106

Wn.2d 557, 565-66, 723 P.2d 1131 (1986). In that case, Weyerhaeuser sold timber under contracts that required a down payment with the balance to be paid in installments without interest. *Id.* at 564. Weyerhaeuser then reported the contract price as gross proceeds taxable under a wholesale rate. *Id.* Pursuant to SEC regulations and generally accepted accounting principles, Weyerhaeuser "internally computed an interest component" and recorded a portion of the revenue as interest for federal tax purposes even though "the contract[s] did not specifically provide for interest." *Id.* at 564-65. The Department imputed this segregated component to Weyerhaeuser and taxed it as if it were interest. *Id.* at 565. This Court voided the Department's actions, holding that it had no authority to impute interest since the sales contracts did not provide for interest. *Id.*

Consistent with this Court's decision in *Weyerhaeuser Company*, the Missouri Supreme Court has rejected the same "substance over form" theory in the context of Flight Options' fractional ownership program in a case involving one of the very same jets that the Department has assessed here. *Fall Creek Constr. Co., Inc. v. Dir. of Revenue*, 109 S.W.3d 165, 170 (Mo. 2003). Critically, in arriving at its decision, the court relied upon the exact same contract provisions at issue in this case. *Compare Fall Creek*, 109 S.W.3d at 170, *with* CP 129, 136, 191. The court determined that this contract language "clearly and unambiguously demonstrate[d]" that the fractional owner was "purchasing an interest in tangible property – the aircraft." *Fall Creek*, 109 S.W.3d at 170. As a result, the court rejected the argument that the "essence" of the contracts

should be viewed as "merely represent[ing] the right to use any aircraft in the interchange program for a specified number of hours per year."[5] *Id.*

Construing the controlling contracts in this case, as required under *Weyerhaeuser Company* and applied in *Fall Creek*, Flight Options is not a "common carrier" subject to taxation as an "inter-county public utility." An essential element of RCW 84.12 is that the utility must be engaged in the public service business of "transporting persons and/or property for compensation." RCW 84.12.200(3). Flight Options' Purchase Agreement demonstrates that it is in the business of selling fractional ownership interests in jets to and managing those jets for the fractional owners. *See* CP 129, 136. Flight Options is not a public airline in the business of providing transportation services for compensation.

Flight Options is not an entity subject to taxation under RCW 84.12. In Washington, most property taxes are assessed by the county assessor of the county where the property is situated. RCW 84.08.010; RCW 84.40.030. The Department possesses limited authority to assess property taxes against those inter-county public utility companies specified in RCW 84.12 whose property is situated in multiple Washington counties. *Northwest Imp. Co. v. Henneford*, 184 Wn. 502, 512, 51 P.2d 1083 (1935) (utility with property in only one Washington county not subject to assessment).

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[5] In its summary judgment briefing, the Department made this same argument, which the Missouri Supreme Court rejected. CP 105 ("[T]he only right program participants acquire when they purchase a fractional interest is the right to a specific number of flight hours.")

This Court has determined that the Department's authority to assess property taxes under RCW 84.12 is limited to public service businesses. *Weyerhaeuser Timber Co. v. Henneford*, 185 Wn. 46, 51, 53 P.2d 38 (1936). In *Weyerhaeuser Timber*, the Department attempted to centrally assess Weyerhaeuser as a "logging railroad company" due to its operation of a private inter-county logging railroad. *Id.* at 46-7. Weyerhaeuser asserted that since all of the companies listed in RCW 84.12 were public utilities subject to state regulation, the Department's authority should extend only to those companies possessing a "quasi-public" element. *Id.* at 48-9. The Department argued that the statute granted it authority to assess "any logging railroad company" and that Weyerhaeuser's operation of a logging railroad was sufficient to subject it to taxation under this statute. *Id.* at 51. Characterizing the Department's position as "illogical and fallacious," this Court held that "[t]here can be little doubt but that the Legislature deliberately intended . . . to include only such logging railroads as had become quasi public carriers by holding themselves out as such carriers." *Id.*

Similar to the Department's insistence in *Weyerhaeuser Timber* that the words "logging railroad company" expanded its taxing authority, the Department has attempted to assess Flight Options in this case under RCW 84.12 based on the presence of the word "managing" in the definition of public utility airplane companies. RCW 84.12.200(3). This emphasis on a single word, taken out of context, is contrary to fundamental principles of statutory construction. *State v. Roggenkamp*,

153 Wn.2d 614, 623, 106 P.3d 196 (2005) ("[A] single word in a statute should not be read in isolation.")

Moreover, like Weyerhaeuser's logging railroad operation in *Weyerhaeuser Timber*, Flight Options' fractional jet ownership program is not a public service business. As discussed above, Flight Options' contracts support this conclusion. Faced with the same argument raised by the Department here, the Missouri Supreme Court rejected the notion that the "essence" of a fractional jet ownership program was for the provision of transportation services. *Fall Creek*, 109 S.W.3d at 170. By contrast, the court found that the fractional owner, Fall Creek, "unambiguously purchased an undivided fractional ownership interest in two aircraft as evidenced by the purchase agreement. The mere fact that it entered into additional management agreements with Raytheon does not change the nature of Fall Creek's ownership interest." *Id.* Since Flight Options is not a quasi-public carrier that held itself out as a public source of transportation for compensation, the Superior Court erred in upholding the assessment of property taxes against Flight Options under RCW 84.12.

This Court has explained that the purpose of RCW 84.12 is to allow for uniform valuation, and allocation, of the value of a public utility company's property when it is spread among multiple counties.[6]

[6] Moreover, RCW 84.12 does not establish an independent basis for imposing Washington State property tax on property that would otherwise not be taxable. Rather, the statute merely grants the Department the limited authority to centrally assess the property of specified inter-county public utilities in lieu of multiple, likely non-uniform assessments by the various counties in which the property is situated. In other words, RCW 84.12 does not tax the business activity of public utilities – most public utilities

Northwest Imp. Co., 184 Wn. at 512. Thus, Washington law requires that the Department "***shall*** apportion such value to the respective counties entitled thereto." RCW 84.12.350 (emphasis added). However, the Department allocated the tax proceeds from its 2005 and 2006 assessments of Flight Options exclusively to King County even though the flights that the Department relied upon to justify its assessments landed at, or took off from, airfields in at least fifteen Washington counties. CP 36-38. This disconnect between the Department's proffered position and its actions helps to illustrate that the Department is merely attempting to extend its powers under a novel (and improper) theory.

As this Court concluded in *Weyerhaeuser Timber*, Flight Options believes that there is "little doubt" the legislature did not intend RCW 84.12 to provide for the central assessment of property tax on persons engaged in non-public service businesses. And yet, to the extent that any doubt exists as to the scope of this statute, this Court has recently reiterated its long-standing rule that "[a]mbiguities in taxing statutes are construed 'most strongly against the government and in favor of the taxpayer.'" *Qwest Corp. v. City of Bellevue*, 161 Wn.2d 353, 364, 166 P.3d 667 (2007) (en banc) (quoting *Estate of Hemphill v. Dep't of Revenue*, 153 Wn.2d 544, 552, 105 P.3d 391 (2005)); *Agrilink Foods, Inc. v. State Dep't of Revenue*, 153 Wn.2d 392, 396-397, 103 P.3d 1226 (2005) (en banc) ("'If any doubt exists as to the meaning of a taxation

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whose property the Department centrally assess under RCW 84.12 are also subject to a Public Utility Excise Tax on their utility business activities. RCW 82.16.

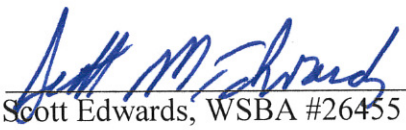
statute, the statute must be construed most strongly against the taxing power and in favor of the taxpayer.'") (quoting *Ski Acres, Inc. v. Kittitas County,* 118 Wn.2d 852, 857, 827 P.2d 1000 (1992)); *Weyerhaeuser Timber*, 185 Wn. at 51 (same). This rule applies "no less when interpreting facts in a tax case and concluding therefrom the applicability of a taxing statute." *Foremost Dairies, Inc. Tax Comm'n*, 75 Wn.2d 758, 763, 453 P.2d 870 (1969).

CONCLUSION

For the foregoing reasons, Petitioner Flight Options respectfully requests that the Court reverse the Superior Court's grant of summary judgment for the Department of Revenue and direct that summary judgment instead be entered in favor of Flight Options.

RESPECTFULLY SUBMITTED this 2nd day of March, 2009.

PERKINS COIE LLP

By: 
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CERTIFICATE OF SERVICE

I certify that a copy of Petitioner Flight Options' Opening Brief was hand delivered via messenger to:

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I certify under penalty of perjury under the laws of the state of Washington that the foregoing is true and correct.

Dated this 2nd day of March, 2009.

Theresa A. Trotland

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